RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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GOLD'S Low-Risk Buy Index turned up last week, rendering a gold buy signal (see Gold Section).

MANIA MARKETS: History tells us that "mania markets" tend to be dangerous markets. I've talked a lot about the mania that has enveloped the markets all during 1993 -- I'm referring to the massive, mind-boggling buying of mutual funds (you can now have your pick of 4,300 different funds with new ones being introduced literally every week).

Now we have a second mania -- it's the buying of anything connected with the "total communications" concept and the "wired home." The merger of Bell Atlantic with Tele-Comunications evidently triggered this new mania (although it was already stirring with merger talk regarding QVC, Paramount, etc.). But suddenly, "investors" are in a frenzy to buy anything having to do with communications or non-wires or entertainment from Baby Bells to Disney.

But wait -- there's a third mania. It's the Initial Public Offering (IPO) mania. "Investors" and speculators will buy ANYTHING that's offered, and I mean anything -- would you believe Uncle B's Bakery (bagels) and Vermont Teddy Bear (stuffed teddy bear); these are actual new issues.

So we have three manias going simultaneously. You can't say it's not interesting.

THE MARKET: I have a habit (gained over 40 years of watching markets) of zeroing in on what's right and what's wrong with the price action. Right off the bat I can tell you what's right with this market. The Dow Industrials and Transports keep pushing up and up. The S&P 500 is hitting new highs along with the NYSE Composite, the NASDAQ, the AMEX and the Wilshire. C'mon, it doesn't get any better than that.

Furthermore, the incredible "Buying Stampede" (as measured by the advance-decline ratio) remains in force -- incredible because the Stampede is now one year old, and no other Buying Stampede in history has ever lasted this long. Finally, my Primary Trend Index (PTI) continues to rally to new highs (see page 2 chart). You can't have a bear market while the PTI is climbing to new highs. It's as simple as that.

OK, is there anything wrong with this market? What's most "wrong" with this market is simply overvaluation. The chart on page 2 tells the overvaluation story. This chart is courtesy of *Investment Quality Trends* here in La Jolla. The upper channel line on the chart represents the 3% dividend yield line (overvaluation), while the lower channel line represents the 6% dividend yield line (undervaluation). You'll note that the Dow has now surged far above the 3% dividend yield line. The only previous instance that was this flagrant occurred in 1987.

So there you are. If one picture is worth a thousand words, this picture is worth at least a single word. That word is "overvaluation."

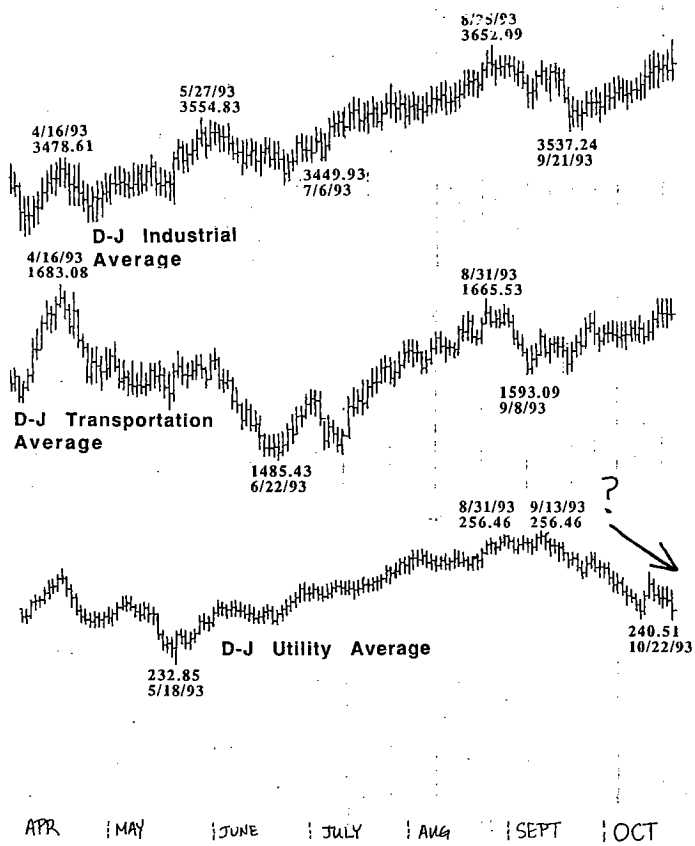
But there are also a few flies in the technical ointment. The first is the recent trend of the D-J Utility Average, which sagged all through September and October. The Utilities, historically, have been one of the first "messengers" of danger ahead. So this could be something worth watching.

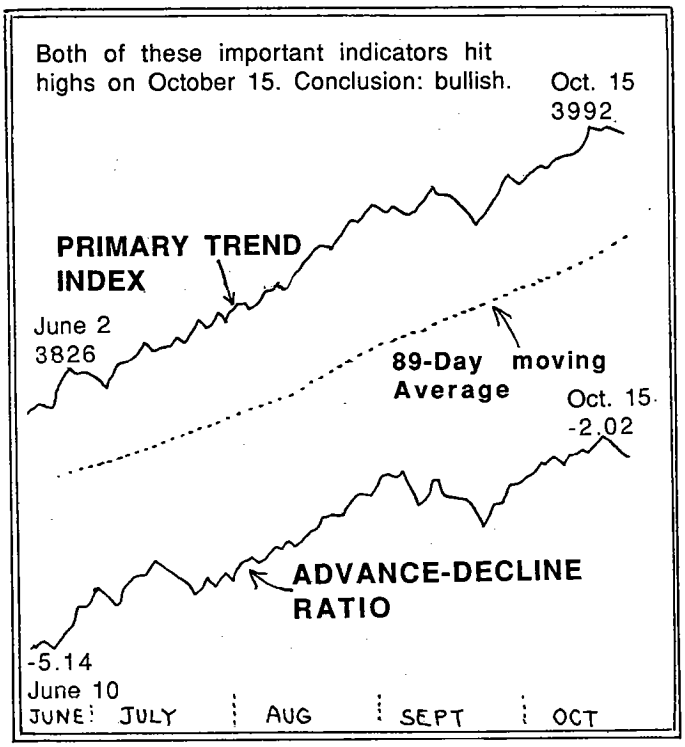
Oct. 15 DJIA 3629.73; PTI 3992; A-D Ratio -2.02
Oct. 22 DJIA 3649.30; PTI 3987; A-D Ratio -2.34
Dow Yield: 2.79%; Dow Price/Earnings: 40.4
Dow 200-day MA: 3483; Dow 30-day MA: 3593
Dow Times Book Value: 3.18; PTI 89-day MA: 3925
Percentage of Undervalued Blue-chips: 8%
Low Risk Buy Index: +73; Gold-PTI: 1115

The second problem is the non-confirming Transportation Average. Remember, the Transports hit their high of **1683.08** back on April 16 (see page 1 chart), and they have not bettered that point since. So that's another item worth watching.

A non-confirmation by the Transports, a downtrend in the Utilities, gold in a slow-building bull market (see page 6), stock yields dangerously low, a public mania to accumulate mutual funds. The trend of the market is up, but the atmosphere has turned rather bubbly. So we'll watch the whole situation carefully.

Note: the Dow is currently trading at a very fat 43 times earnings. But analysts are predicting total Dow earnings of $255 next year. On that basis, the Dow is selling at 14 times future earnings. The big question: can the Dow really earn $255 next year? *Forbes* (Oct. 25) in a piece entitled "Wait Until Next Year" notes that the analysts have been notoriously poor on predicting earnings. Plus they can quickly revise earnings both up and down. So until proved otherwise, the Dow must be considered to be very expensive on a price/earnings basis. That is, of course, unless this time the analysts are right.





QUESTIONS: Will the economy pick up or won't it? Will inflation return again or won't it? Will the stock market correct or won't it? Will the bull market continue or won't it? Will Clinton's health bill pass or won't it? Will NAFTA pass or won't it? Will Bill Clinton be a one-term President or won't he?

What is it that the Zen master said? Oh yes, I remember. He said, *"One fool can ask more questions than 10 wise men can answer."*

Every day I play the fool with myself in that I ask myself a lot of unanswerable questions. You see, it's a lot easier to play the fool than it is to play the wise man.

Let's go backwards for the answers. I believe Clinton will be a one-term President. I am doubtful that NAFTA will pass. A health bill? I'm guessing, maybe 50/50, that some kind of a national health bill will pass, but it won't be the program that the Clintons and their 500 experts have come up with.

Will the bull market continue? A guess -- I'll be surprised if it lasts another six months. I'll be amazed if we get through 1994 without a major bear market starting. What would trigger a bear market? My guess, it will be triggered by either trouble from interest rates (i.e., falling bonds and rising interest rates), or trouble on the dollar front (brought on by the unending deficits). Often, the market will have discounted the BEST that lies ahead, at which point stocks drop of their own weight and a bear market begins.

Will the stock market simply correct in lieu of a bear market? Maybe, but my guess is that the next important downturn won't be just a correction, it will be the start of a bear market. I base that on (1) overvaluation in the market, (2) the extraordinary extent and duration of the rise since 1974, which is when I believe this bull market started, and (3) this bull market has moved into the mania stage, not the least of which is the massive movement of the public into 4,300 assorted mutual funds.

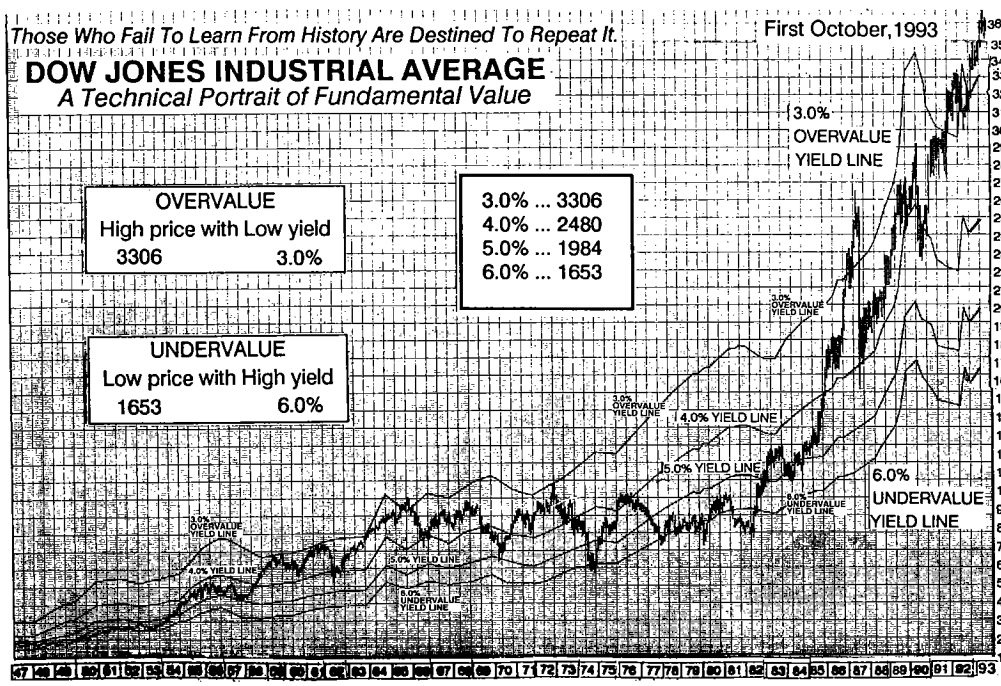
Next question: Will the US economy pick up or won't it? At this point in the game, I really think it's up to the stock market as to what happens in the economy. If the stock market continues to push higher, or even go sideways, I think business may get better, maybe not a lot better, but better.

However, if the stock market topples over and a bear market starts, forget better business, it won't happen. With one out of every four families owning mutual funds, a bear market would dry up consumer spending in a hurry. On top of today's high and continuing unemployment, a stock market collapse would knock the US economy on its fannie. It would probably knock the world's economies flat to boot. To put it succinctly, from here on everything depends on the markets.

Nobody (including the Fed, it seems) looks at the money supply figures any more, but I do. This from the *St. Louis Fed* (Oct. 7): *"The M-1 money supply has expanded at a 13.5% annual rate since June, compared with a 9.3% increase during the previous six months."* So you can't say that the Fed hasn't put the pedal to the metal. It's going all out in an attempt to reflate the US economy (so far, all they've reflated is the stock and bond markets).

But I also notice that M-3, the broad measure of money supply has started to expand. M-3 has risen in three out of the last four weeks. This means that the banks are starting to pick up their lending. And if bank lending expands, that's a definite plus for the economy.

For price action, see Late Notes (page 6).



INVESTMENT POSITION: I believe we're looking at a grandpa bull market in stocks. Now there's nothing wrong with a grandpa (I'm one myself, actually three times over), but to be truthful, I'd rather bet on youth. I believe the bull market in gold is a youthful one, and that's where I've put my money (yep, I still call dollars money).

For gold stocks I like Placer Dome, Amer. Barrick, Pegasus, Homestake, Echo Bay, Agnico-Eagle, Royal Oak, and Franco Nevada (last one on the Toronto

exchange). I also like the gold coins, and the less premium over actual gold content the better. So that means krugerrands, which sell at a very slight premium over gold content, sometimes as low as 1%.

Yes, I know that a lot of people have made money in new issues and communications issues and hot merger issues and what have you. But you can't be all over the place, so I'm sticking with gold. Furthermore, I always think in terms of risk vs. reward, and I believe the best long-term risk/reward situation at this time is in gold.

Remember, I also believe that we're moving into an era where there will be a growing movement into real (tangible) items and out of financial items. Financial items (stock and bonds) are historically very expensive whereas tangible items (specifically golds) are cheap.

Back in 1980 the price of gold crossed over the price of the Dow. I believe that somewhere ahead we'll see that same phenomenon again. Sound crazy? Maybe, but I believe it will happen.

CURRENCY HISTORY: I've been wanting to run a series on the history of the major currencies. I feel this study will provide an important and timely background for my subscribers -- particularly in this age of fiercely competitive currency devaluations.

So let's start with that modern powerhouse, the German D-mark. The mark came into existence a thousand years ago as an unit of weight -- a half pound of silver being equal to one mark. Today that half pound of silver would be worth around 65 dollars. But that was the old Teutonic D-mark. The modern mark was born in 1871. At that time one D-mark was worth 23.8 cents in US money.

The mark held generally to its 1871 value until World War I. When the War started, Germany went off the gold standard as did many other nations. As war expenses exploded, Germany entered the money-printing business. In 1914 at the beginning of the War, the mark was valued at 4.2 D-marks to the dollar. Inflation, brought on by huge war debts, continued to ravage the mark. By 1923 it took 4.2 trillion marks to buy one dollar. The value of the mark and all German savings were effectively wiped out.

In 1924 Germany came up with what we might call a reverse currency split. At that time Germany announced that 1 trillion of the old marks would be worth one new mark. But when Hitler came to power and many Germans began to realize what a Nazified Germany would mean, D-marks started to flee the country. The flood of marks became a torrent. In late-1936 Hitler announced a shocking new edict -- the death penalty for anyone who exported marks. When WWII ended and Hitler's Third Reich collapsed, the mark again sank to nothingness. This was the D-mark's second disastrous wipeout in 23 years.

In 1948, amid vows that Germany would never again go through the agony of a mark inflation, the modern D-mark was born. At that time the mark was worth 33 US cents. But by 1951 the new mark sank to a record low of 12.4 cents.

Then the German "production miracle" began. German efficiency and know-how came to the fore. Germany was fast becoming an industrial powerhouse. By the early 1960s German goods were being exported throughout the world. In 1961 the D-mark climbed to 25 cents in US currency. By 1969 it was 27.3 cents. By 1991 the mark rose to a record high of 69.44 cents. As this is written, the mark is worth about 60 cents. From its low point in 1951 to its high point in 1991, the D-mark had risen 460% against the dollar.

The German central bank, the Bundesbank, is bound by its charter to defend the value of the D-mark. The Germans, having seen their currency and their wealth wiped out twice, will take a recession, a depression, anything rather than another inflation and wipeout of the mark.

The paradox -- Americans, having been traumatized by the Great Depression of the 1930s, seem to be willing to have the value of the dollar wiped out rather than take another depression or even a deep recession.

All of which takes us to 1993, the year that saw the European Rate Mechanism (ERM) fall apart. Why did it fall apart? One reason it collapsed was because Germany's central bank, the Bundesbank, refused to drop their interest rates fast enough or far enough to suit the many recession-wracked nations of Europe.

A brief comment about the Bundesbank. The bank was modeled after the US Federal Reserve. The chief duty of the bank, according to its 1957 charter, is that of "safeguarding the currency." The 16-man board of the bank is appointed by the German Federal President and serves in office for eight years. They cannot be removed by government. The Bundesbank is non-political and is the most independent central bank in the world.

That's a brief story of the mark, and my thanks for a good deal of the background for this piece to Chris Weber and Leonard Reiss, authors of the book, "Getting Rich Outside the Dollar".

NOTES & QUOTES: Everyone who writes or calls wants to know, "Russell, are you OK?" Answer: "Yes, I'm OK -- actually, I feel fine." And I've got confirmation. According to the Nuclear Medicine Dept. of Scripps Memorial Hospital here in La Jolla, I'm OK. How do they know? 10 days ago I took a "Thallium Treadmill" test. How does that work? Well, here we go with modern medicine again. First they inject you with Thallium which is a radio-nuclear drug. "Will I set off a Geiger counter?", I asked. The technician smiled and said I might. Next, you lie down on a narrow table, and a huge, space-age-looking electronic camera moves slowly back and forth across your chest. It does that for a full 20 minutes. Then they trot you off to another room, and you get on a treadmill (they inject you again with another substance called Mivi). While you're on the treadmill your cardiologist checks your vital signs. You tread as far and as fast as you can -- until you're exhausted. An electrocardiogram records your heart rhythm. Then it's back for another 20 minutes on the table with that monster camera scanning you.

They put all the pictures together along with your treadmill results. What they're looking for among other things is ischemia or constricted blood vessels. In other words, are all parts of your heart getting enough blood and oxygen? A day later they handed down the verdict. I'm all right. Science marches on, taking Richard Russell with it.

* *

I'm convinced that I have the world's most interesting subscribers. Here are a few paragraphs from a letter by John Shuttleworth (he's the founder of *The Mother Earth News*): "I'm sure you saw the little article about the 'reachback taxes' on the editorial page of the *WSJ* yesterday. Absolutely frightening! Anyone can have everything taken away from him or her under that reasoning. 'Oh, you were in the coal business 30 years ago. Well, we have just decided that your company didn't pay enough taxes three decades ago, so we're assessing you $250,000 a year from now in back taxes. It's only fair.'"

John also talks about maybe the greatest appreciating asset since WWII. He writes, "Jim Rice, then manager of the Van Wert, Ohio, airport (this was about 1957) bought a brand new P-57 (Mustang) surplus fighter -- plus a brand new Rolls Royce extra engine in the original cosmoline and original crate -- all for $500, total. My new issue of TRADE-A-PLANE says I can now buy a P-51 for anywhere from $550,000 to $625,000 and up." Russell comment: I'd call that appreciation. The P-51s were beautiful, long range and very fast. They are still used in racing: Herman Goerring, head of the German air force, wrote that when he saw the heavy bombers coming over Berlin with the P-51s flying cover, that's when he knew the war was lost for Germany. Personally, I knew the war was won for the Allies when on bombing missions we didn't see a single German fighter plane coming at us (I was a bombardier on B-25s in the Twelfth Army Air Force).

* *

Back in the '50s and '60s Fed Chairman Alan Greenspan was a disciple of that fierce capitalist, Ayn Rand (she wrote "Atlas Shrugged" and "The Fountainhead"). Greenspan knows gold, and in 1966 he wrote, *"The abandonment of the gold standard made it possible for the welfare statists to use the banking system as a means to an unlimited expansion of credit. In the absence of the gold standard, there is no way to protect savings from confiscation through inflation . . . Deficit spending is simply a scheme for the 'hidden' confiscation of wealth. Gold stands in the way of this insidious process."* Later Greenspan bad-mouthed the Fed because it abolished the pure gold standard.

Question: In view of the above, did Greenspan sell-out? Russell opinion: I think Greenspan loves the sheer power of being Fed Chairman. He also (obviously) decided to live with the Fed, and he's probably doing his best within the context of a system which he once railed against. But yes, I believe Greenspan did sell out. If you don't believe in the Fed, you don't head it, you speak out against it. And where is Greenspan on gold? Not a word on gold from the Fed Chairman.

* *

This from economist E. Erich Heinemann of Ladenburg, Thallmann (he's an expert on money and the Fed): "The Fed pumped more than $1 billion in fresh reserves into the banking system in September. This was part of a continuing pattern. Over the past three years the Fed added almost $20 billion to total bank reserves -- 'high powered money.' That was an average gain of about 12.75% . . . Long term relationships show that sustained accelerations and decelerations in bank reserve growth affect inflation with a lag of about three years. Actions the Fed has already implemented indicate that core inflation will increase from about 3.25% at present to more than 5%. Our work shows that if the Fed's current policy of 15% reserve growth continues, then inflation will range between 6% and 8% by mid-decade." Russell comment: And you wonder why a bull market in gold is underway!

Heinemann on the Clinton health plan: "Do not be deceived by the fancy rhetoric wrapped around Bill Clinton's plan to reshape delivery of health care services. It is mostly just one more large tax increase. We believe that the net cost in higher explicit and implicit health-care taxes is likely to be over $125 billion over five years."

* *

Facts: I just computed the total additions to the national debt that have built up during the last 12 months. The figure is **$353 billion.** If anyone is cutting the deficits, it isn't showing in the actual figures. We're still running deficits of approximately $1 billion a day.

* *

Thanks to my old friend, Kennedy Gammage (he publishes the excellent *Richland Report* out of La Jolla) for the following:

> Columnist Pat Buchanan through his organization "The American Cause" has retained Washington constitutional attorneys Michael George and Alan Dye of the law firm Webster, Chamberlin and Bean to challenge Congress and the Administration regarding the recently enacted retroactive taxes. We will be sending a contribution to assist in this worthy effort, because (1) we believe his lawsuit has an excellent chance, and is in the right; and (2) if we win, and the taxes are repealed (as we feel they clearly should be on constitutional grounds), we'll be repaid in an amount greater by far than our contribution.
>
> If you read Article I, Section 9, Clause 3 of the Constitution, it clearly states that Congress shall pass no *ex-post facto* (i.e., retroactive) laws. It's unambiguous and explicit. And the 5th Amendment gives citizens the right to challenge any such laws -- again, clear and unambiguous.

Russell comment: To me, the retroactive boost in taxes is an absolute outrage. And I also believe it's unconstitutional. It's all part of the Clinton war against "the rich." Be prepared for more.

* *

Yoshiro Nakamatus just gave a free lecture in San Diego. The lecture was on creativity and technology. Who is this guy? He's a genius and is called, "The Einstein of Japan." Yoshiro invented the floppy disk, the digital watch, and get this -- he holds 2,360 patents.

* *

Believe it or not, some good things are happening in the USA. One is the return of the bison. After a 120-year absence, a herd of 300 of the thundering beasts have been placed on a 36,000 acre preserve in Pawhuska, Oklahoma. The herd is expected to grow to 1,800 buffs. Said Gen. H. Norman Schwarzkopf, who was present at a ceremony, "This is a gift for future generations . . . the great-grandchildren of the children here today can see what our grandparents saw." Russell comment: What our grandparents saw were huge herds of buffaloes, herds that roamed the prairies from Texas to as far north as Canada.

* *

Shocking statements from Japan, specifically from Hiroshi Kumagai, powerful Minister of International Trade and Industry: *"Big business in Japan is a hotbed of collusion. We need radical reform of the Japanese economy. If Japan's trade surplus continues, it will be one of the factors leading to the destruction of the world economy."* Tough words, but will or can Japan change? Washington has been hoping that the strong yen would depress Japan's massive trade surplus. Not yet, it hasn't. Japan's current account surplus (the broadest measure of its trade), widened 7.4% to $7.23 billion in August. That was a record for the month and the 29th consecutive month of expansion. The powerhouse yen, which has climbed by 20% against the dollar this year, has not slowed the Japanese trade surplus. Moreover, the high-priced yen is now hurting the Japanese economy, and that in turn has cut into Japanese imports. Still, nothing seems to cut into Japan's surplus. Japan's gathering recession could bring the yen down (remember, the stronger a nation's economy, usually the stronger its currency, and Japan has sunk into recession). The sinking yen will not make the US happy -- Washington would like a cheap dollar and a super-high yen.

* *

How are things in La La land? Not really that great. This from the October 8 *LA Times: "Already confronted with the gloomiest picture ever, Los Angeles County officials report that home owners are contesting property valuations at such a furious rate that they threaten to overwhelm the appeals process, potentially cutting into the county's tax revenues."* Russell note: *Dataquick* of San Diego states that since 1990 nine out of 10 homes in Southern California have lost value. Interestingly, one of the few appreciating real estate areas is Borrego, about an hour and a half east of San Diego on the desert. People are moving away from the big cities and even away from the suburbs. A friend of mine, an ex-American Airlines pilot, bought a plane a few months ago, and flew "about everywhere," looking for an ideal place to relocate. He picked St. George, Utah, a town of about 45,000. "Clean streets, clean air, modest home prices, good folks, no gangs."

* *

A new book just published is entitled,*"The Endangered American Dream,"* author Edward Luttwak. He predicts that the way we are going, by the year 2020 the US will be a Third World nation. This from a *Business Week* review about the book, "Consider, for example, what a visitor from Japan or Europe will encounter upon arriving, say, at Kennedy airport. Compare the clean, computerized efficiency of Narita or Schiphol or Frankfurt International with the frayed carpets, broken escalators, naked plywood, and unfinished gypsum-board walls of JFK. What we have here, writes Luttwak, is a worm's eye view of the 'deferred maintenance' by which America has been relentlessly consuming rather than renewing its invested capital. Result? A country acquiring Third World street scenes with their dilapidated buildings, broken pavements, crudely painted boardings, and decrepit buses.' These are shocking observations for anyone accustomed to thinking of the US as the richest nation on earth. But to stay rich, a country must invest in itself, and over the past 30 years Washington has consistently pursued policies that pay lip service to investment while actually encouraging consumption and even outright disinvestment."

Russell comment: The US is a nation with an extremely low savings rate (3.75%) and extremely high debt, and the debts keep growing. No currency can hold up under those conditions, and thus the long-term trend of the dollar continues to be down.

Furthermore, no other nation can get away with what we've been getting away with. The US continues to sell its debt to foreigners and then pay them back with its own depreciated dollars. How long can this go on? How long will our creditors continue to buy and hold US paper that is depreciating in value? This could be the number one question of the '90s.

* *

Do central banks speculate on currencies? You bet they do. In fact, *Futures* magazine (October) calls central banks "the ultimate inside traders." Central banks usually want the market to know when they are intervening in order to bolster a currency. Central banks like their foreign reserves to show a profit, although the banks are above all concerned with liquidity (liquidity is needed for interventions). Negara, the central bank of Malaysia, has long been known as a major currency player. But in 1992 the bank's contingency reserves sank by $3.72 billion, a drop of 90%. During 1990-91 the central bank of Mongolia lost $80 million on foreign currency speculation, literally wiping out this formerly Communist country's reserves. Mongolia's dealers (some still in their teens) held a $1 billion position and kept up with the currency markets by using a single telex machine and operator-assisted phone calls. The former governor of the Mongolian central bank is now on trial.

* *

I often mention legendary billionaire investor Warren Buffett (Berkshire Hathaway). But few of his many admirers are aware that Buffet's dad, Howard Buffett, was a US congressman from Nebraska. Howard Buffett was also an ardent advocate of the gold-backed dollar. And when the US went off gold, I imagine that his son, Warren, knew what this would mean. It would mean inflation as far out as the eye can see. Which may be why Warren continues to buy corporations (he'd rather have companies than dollars). I happen to have a pamphlet which contains dad Buffett's speech on gold and freedom. Warren, if you happen to be reading this, here's what your pop thought:

Human Freedom Rests on Gold Redeemable Money

By HON. HOWARD BUFFETT*
U. S. Congressman from Nebraska

Congressman Buffett stresses relation between money and freedom and contends without a redeemable currency, individual's freedom to sustain himself or move his property is dependent on goodwill of politicians. Says paper money systems generally collapse and result in economic chaos. Points out gold standard would restrict government spending and give people greater power over public purse. Holds present is propitious time to restore gold standard.

Is there a connection between Human Freedom and A Gold Redeemable Money? At first glance it would seem that money belongs to the world of economics and human freedom to the political sphere.

But when you recall that one of the first moves by Lenin, Mussolini, and Hitler was to outlaw individual ownership of gold, you begin to sense that there may be some connection between money, redeemable in gold, and the the rare prize known as human liberty.

Howard Buffett

Also, when you find that Lenin declared and demonstrated that a sure way to overturn the existing social order and bring about communism was by printing press paper money, then again you are impressed with the possibility of a relationship between a gold-backed money and human freedom.

In that case then certainly you and I as Americans should know the connection. We must find it even if money is a difficult and tricky subject. I suppose that if most people were asked for their views on money the almost universal answer would be that they didn't have enough of it.

In a free country the monetary unit rests upon a fixed foundation of gold or gold and silver independent of the ruling politicians. Our dollar was that kind of

*An address by Congressman Buffett before the Conference of American Small Business Organizations, Washington, D. C., May 4, 1948.

* *

I've talked about the "virtual corporation" before. The idea is catching on, and the Clinton medical program will only make the VC more popular. This from economist Robert Kuttner: *"An increasingly trendy concept is the virtual Corporation. The idea is that companies should have a core of owners and managers, but, to the greatest degree possible, workers should be contingent -- temporary, part-time, or on short-term contracts. This gives the corporation maximum flexibility to shift vendors, pare costs, and avoid long-term labor commitments."* Russell comment: Let's put it bluntly -- corporations today are in a frenzy to get rid of as many workers as they can, and that includes managers. The virtual corporation is a concept whose time has come, a company without workers.

* *

With many stocks pushing far into the overvalued area, it becomes highly attractive for a company to buy another company with stock, rather than with cash. Thus Berkshire Hathaway just bought Dexter Shoe Co. with $400 million in Berkshire stock. As for the REALLY BIG merger of Bell Atlantic with Tele-Communications Inc., Bell will issue 220 million shares ($11.8 billion) of a new class of stock worth about $54 a share. When times are rough and people are careful, it takes cash to buy a company. When stocks are highly inflated (sky-high P/E ratios), instead of cash, you buy another company with more of your own stock. Watch for a lot more of these deals -- as long as the markets stay bubbly.

* *

Health: One of the latest theories on aging is that just as a car engine generates poisonous fumes when it burns fuel, so the body generates harmful by-products as it burns energy. Each day the body generates around 10 billion "free radicals," a natural process of breathing and digestion. Many biochemists now believe that free radicals are one of the prime cell killers in the process of aging. What does the body do to protect itself against free radicals? It produces antioxidants, substances which attack free radicals. But as people grow older, their production of antioxidants diminishes and the cells are ultimately overwhelmed. But wait -- the latest thesis is that the following can actually inhibit free radicals: vitamins C and E, beta carotene, L-carnitine, coenzyme Q-10, plus vegetables and fruits. All of these items can be obtained at your local "health food" store, and most of these same stores carry literature on antioxidants. So the vegetarians and "health nuts" may not be crazy after all.

* *

Words to ponder: *"I can do anything now at age 90 that I could do when I was 18. Which shows you how pathetic I was at 18."* -- George Burns.

From oil man Jerry Jones who owns the Dallas Cowboys: *"If you're in the oil business, you learn to expect bad news. And that helps me here, because there's a lot of bad news in football, too. You gotta expect injuries. Remember, it's unnatural playing football. God tells you to run away from a 275 pounder -- not into him. So they're heroes, players are, sure, but in the end they're just gladiators."*

* *

The total number of pages in the Federal Register tends to dovetail with the trend of inflation. In 1992 the Register contained 65,000 pages. But this year the Register boomed to 86,000 pages (a level not seen since Jimmy Carter was in the White House). The theory -- the more pages in the Register, the more government -- and the more government, the more inflation.

* *

Suddenly, we have coffee houses all over La Jolla. Everybody's drinking the caffeine-charged brew -- except me. I'm allergic to it, and one cup of even a decaffeinated coffee (and even decaffeinated does have a small amount of caffeine in it) will drive me up the wall. So suddenly we have a new glamour stock, the successful Starbucks chain of coffee houses (NASDAQ). But wait a minute. Now Chock Full o' Nuts is planning to open their own chain of coffee houses in '94 (they'll be sleek, European espresso types). I remember when Chock Full first started in the early '50s. They came out with a delicious sandwich of cream cheese on nut bread -- all for a bargain price of (would you believe) 11 cents. And their great coffee was a nickel a cup. Later, hard times hit old Chocky and the company faded from view. And now -- another chain of coffee houses. Does America need it? I don't think so, but I could be wrong. Listen, Americans need to get buzzed on something.

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US Morality: Over the last four years 90,000 people in the US were murdered, half by handguns. In the Vietnam War 58,000 Americans died. Should we outlaw handguns? I say it's far too

late. Criminals and felons don't buy handguns at the local gun store. They steal guns or buy them on the black market. Banning handguns means disarming law-abiding citizens while the criminals have all the guns and the power. Interviews with convicts tell us that the situation that robbers, burglars and muggers fear most is the armed citizen. I say ban handguns for those under 18, make citizens wait 15 days (for a check) before buying a gun, let carefully tested citizens bear concealed weapons, but don't talk about banning guns -- unless you've found a way to disarm America's criminals and crazies first.

GOLD: Question: What's the single most important fact about gold at this time?

Answer: The single most important fact is that *gold is in a bull market.* Furthermore we're in the early stage of this bull market, and I've been warning that in its early stage, a bull market tends to be erratic, deceptive, difficult, often discouraging. This is the stage where the bull tries to shake off its riders; it's the stage where the bull wants to advance while carrying the fewest number of investors on his back.

Later, perhaps a good deal later, we'll see the time when gold will rise relentlessly -- day after day, week after week. At that time we'll look back and wonder how we ever stayed with gold during this difficult and frustrating early phase.

Right now the stock market is in the late stages of a bull market. You can see that in the action of the PTI, which continues to climb day after day. Confirming the PTI action, the advance-decline ratio rises to new highs almost daily. But those of us who invested at the beginning of the great bull market back in 1974 remember that it was darn hard to buy stocks (even though stocks were screaming bargains). And it was just as hard to hold them.

All of which explains why I've worked to develop my new Gold Primary Trend Index (G-PTI). I want to use the G-PTI to boost confidence, to demonstrate to my subscribers what's really going on in the gold market.

I know from experience that the concept of a bull market is the most difficult of all concepts for the average investor to grasp. Why is gold above 370? Why has gold moved up from its February low of 326 when our government tells us that there is no inflation? Why, why?

The only answer you need is that it's a bull market in gold. In due time we'll know WHY there's a bull market in gold. Suffice it to say that there are events coming up which will justify the bull market in gold. Inflation, deflation, a run on the dollar, social chaos, supply/demand -- I'm not sure of the answer. But I do know that large interests are accumulating gold and gold shares. We're seeing it in the action of both the metal and the shares as first one, then the other, lead the way up. The gold bull is slowly getting to his feet. He's still a bit unsteady, he's still tentative, but in due time we'll feel his full strength.

A lot of people have asked, "What would happen to gold in the event of a major deflation? Wouldn't gold get hit hard? After all, gold is basically an inflation hedge."

I've done a lot of thinking on this subject. Of course, we know what happened to gold during the last great deflation, that of the 1930s. In an attempt to reflate and boost reserves, Roosevelt in 1933 raised "the official price" of gold from $20.22 an ounce to $35 an ounce. When asked how or why his people had picked the $35 price, Roosevelt replied sarcastically that his advisors had just shuffled a bunch of numbers around and 35 seemed like a good one.

But it's a different world today; the US is in different circumstances. I believe that if the US economy sank into deflation, the dollar would be in grave danger. In fact, I think there would be a run on the dollar, a run to other currencies (D-mark, Swiss franc, maybe Dutch guilder) -- and also a run to the safety of pure money -- gold.

Why do I say that there'd be a run on the dollar? My answer is that with over $4.4 trillion in federal debt, with continuing federal deficits of $1 billion a day, and with total US debt (including corporate and individual debt) of $15.2 billion, a serious deflation would cause a collapse in the whole US financial structure. Remember, the US economy is built on, and lives on, inflation.

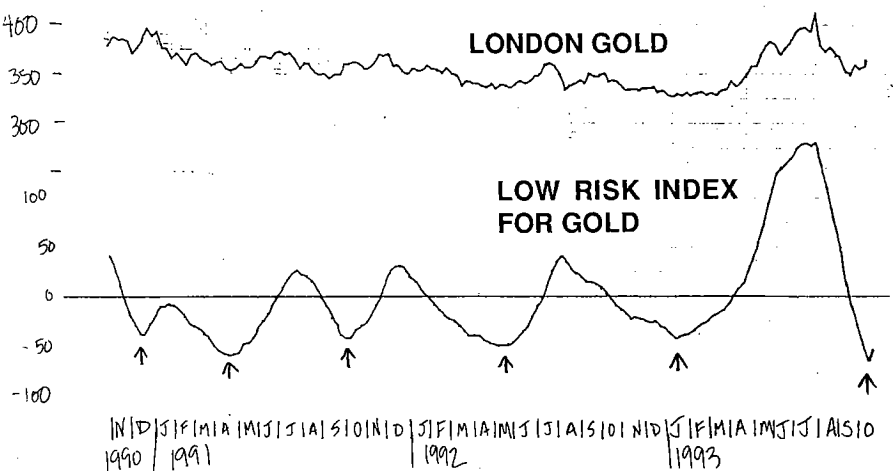
This debt-laden economy could not hold up under deflation, and neither could the dollar. Therefore, I believe that if deflation does take over, the real shocker would be a run on the dollar, and a rush (certainly by international interests and by our foreign creditors) to get out of dollars and into other currencies and into gold.

In the Great Depression of the 1930s everybody wanted dollars. If there is a deflation in the 1990s (and I'm obviously not convinced that there will be one) nobody will want dollars. For while the dollar held up beautifully during the deflationary '30s, I don't believe it would hold up in a 1990s deflation.

Technical: This is my chart of gold and the Low-Risk Index for gold (LRI). Remember, the LRI is used to identify low-risk buying areas. These areas are identified as follows: *when the LRI drops below zero (the lower it drops, the better) and then turns up, at the point where the LRI turns up, that's where we receive our ideal low-risk buying point.*

Two weeks ago the LRI for gold sank to its lowest level in years (far below zero). And I thought it very significant that with the LRI that oversold, the metal continued to hold well above 360. Next, on October 22 gold closed above 370. At that point the LRI for gold turned up. The upturn in the LRI from below zero identified a low risk buying point for gold and gold items.

Once the LRI turns up, it tends to continue up until it is well above the zero level. The important point is this -- the upturn in the gold LRI is just getting underway.



LATE NOTES: The Dow is at record highs with almost all the European indices also at new highs. Could the performances of all these indices be telling us that world economies have seen the worst and are about to turn up? It's certainly possible. My feeling is that it will require tremendous and continuous money creation by the various central banks of the world to offset (or at least fight) the forces of debt and deflation. This is bullish for gold, bearish for bonds. The recent weakness in the US bond market is already putting pressure on stocks here . . . With the US economy seeming to improve, watch for a possible shocker -- the dollar and gold moving up together.

Coming in the next Letter -- my prediction of new world trends.

NEXT MAILING: Nov. 10, 1993